No. 80-881

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MICHAEL RODAK, JR.

In the Supreme Court of the United States

OCTOBER TERM, 1980

TEMA OIL COMPANY AND ASHLAND EXPLORATION, INC.,
PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

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Petitioners contend that the court of appeals applied an improper standard of review and erroneously affirmed the Federal Energy Regulatory Commission's interpretation of one of its own regulations.

1. Petitioners are producers of natural gas which they sell to interstate pipelines for resale in interstate commerce. The rates for such sales are subject to the jurisdiction of the Federal Energy Regulatory Commission under Section 1(b) of the Natural Gas Act, 15 U.S.C. 717(b). This case involves two rate filings made by petitioners pursuant to the Commission's rules authorizing collection of higher rates for gas sold under a contract that has "rolled over," *i.e.*, a contract that has expired and has been replaced by a new contract for the same supply of gas.

a. In 1972, the Federal Power Commission[1] established the so-called "rollover" policy as a feature of its regulation of the rates charged by producers of natural gas. For some time before the adoption of this policy, the Commission had set the rate for producers' sales of gas according to a two-tier pricing system. As the court of appeals explained it (Pet. App. 2a-3a; emphasis in original):

> Under that system, the maximum price for which regulated gas could be sold depended on its "vintage." Gas sold pursuant to a contract entered into *before* a specified "division date" was "old" and was distinguished for regulatory purposes from gas that had not been sold in the interstate market until *after* the specified "division date." That gas was regarded as "new." The ceiling price for "new" gas was higher than that for "old" gas, presumably to cover the higher production cost and to encourage new exploration.

By instituting the "rollover" policy, the Commission sought gradually to eliminate "vintaging" by allowing "old" gas to qualify for the higher "new" gas price when the original "old" gas contract "rolled over." The rollover rule was intended as a mechanism for improving economic incentives for increased production of gas while minimizing economic harm to consumers from higher gas rates.

Under this new pricing scheme, gas produced and sold under contracts signed on or after January 1, 1973, is priced at "new" gas rates even if the gas is produced from fields that once supplied gas pursuant to pre-1973 contracts. In order for gas produced by such fields to qualify for "new" gas treatment, the post-1973 contract must replace an earlier

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[1]In October, 1977, the Federal Energy Regulatory Commission succeeded to the functions and responsibilities of the former Federal Power Commission with respect to the regulation of natural gas sales for resale in interstate commerce under the Natural Gas Act, 15 U.S.C. 717 *et seq.*

"original" fixed contract that has expired of its own terms. If, however, the original contract is of an indefinite duration, *i.e.*, for as long as production from a given well is profitable, it will never be eligible for the "new" gas rate.[2]

b. In 1976, petitioners filed two proposed rate increases pursuant to the Commission's rollover rule. The two filings have the same relevant characteristics: In each instance petitioners entered into a fixed-term contract with an initial buyer. Prior to January 1, 1973, the contract expired of its own terms and petitioners entered into a life-of-lease contract with a different buyer. In 1976, petitioners and the second buyer modified the life-of-lease contract to permit rate increases up to the national rate ceiling as set by the Commission. Petitioners then filed the proposed rate increases with the Commission, claiming that the rate increases were warranted under the rollover rule.

The Commission rejected the rate filings because "the original contracts with the current purchasers have not expired. The fact that the original contracts covering sales from these properties have expired is of no significance here because such contracts covered sales to different buyers * * *" (Pet. App. 17a).

The Commission reaffirmed its ruling on rehearing (Pet. App. 10a-15a), observing that the "identity of purchaser" requirement was contemplated in the Commission's initial formulation of the rollover rule in 1972. In this initial

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[2]The replacement contract policy is currently codified in 18 C.F.R. 2.56a(a)(5), which states that "new" gas rates will apply, provided the sale is made pursuant to

> * * * a replacement contract where the sale was formerly made pursuant to a permanent certificate of unlimited duration under such prior contract which expired by its own term on or after January 1, 1973, or pursuant to a contract executed on or after January 1, 1973, where the prior contract expired by its own terms prior to January 1, 1973 * * *.

formulation, the Commission had stated that the rule would apply when the "purchaser and seller enter into a new contract" to replace the original fixed-term contract (*id.* at 14a).

The court of appeals affirmed (Pet. App. 1a-9a). After a thorough analysis of the relevant regulation and the policies it was intended to further, the court concluded that "the Commission's interpretation of its own regulation is clearly within reasonable bounds" (*id.* at 2a) and in furtherance of one of the regulation's stated policy objectives (*id.* at 8a-9a).

2. The decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court. In affirming the Commission's interpretation of its own regulation, the court of appeals properly applied well-established principles governing the appropriate standard of review of such agency action. See *Ford Motor Credit Co.* v. *Milhollin*, 444 U.S. 555 (1980). Review by this Court is therefore unwarranted.

Petitioners contend (Pet. 5) that the court of appeals applied a "novel" standard of review that essentially precludes a reviewing court from overturning an agency's interpretation of its regulations unless the court concludes that the agency's interpretation is "irrational." This contention misconceives the holding of the court of appeals.

The court's reference to "irrationality" was in answer to petitioners' claim that the Commission's interpretation was contrary to its stated policy objectives, and not to the question whether the Commission's interpretation was inconsistent with the new regulation itself. As to the latter question, the court below expressly relied upon the standard established by this Court's decisions[3]—*i.e.*, that "the agency's interpretation is 'of controlling weight unless it is

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[3] *Udall* v. *Tallman*, 380 U.S. 1, 16-17 (1965); *Bowles* v. *Seminole Rock & Sand Co.*, 325 U.S. 410, 413-414 (1945).

plainly erroneous or inconsistent with the regulation' " (Pet. App. 7a). Applying this standard, the court found (*ibid.*) that the mere fact that there is no express "identity of purchaser" requirement in the regulation itself does not render the Commission's interpretation inconsistent with the underlying regulation. See *Austral Oil Co.* v. *FPC*, 560 F. 2d 1262 (5th Cir. 1977) (sustaining a Commission interpretation of the rollover rule which imposed a requirement not included in the language of the rule itself). The court further found that where, as here, the conflicting interpretations offered by petitioners and the Commission were both reasonable, the agency's interpretation must prevail (Pet. App. 7a-8a).

In rejecting petitioners' claim that the Commission's interpretation conflicted with the policy considerations underlying the regulation, the court below recognized that (Pet. App. 8a):

> [A] " 'presumption of validity . . . attaches to each exercise of the Commission's expertise.' " *Mobil Oil Corp.* v. *FPC*, 417 U.S. 283, 307 (1974) (quoting *Permian Basin Area Rate Cases*, 390 U.S. 747, 767 (1968)). For this reason, only if the Commission's interpretation were so at odds with its stated policy objectives as to render its determination irrational would this court set that order aside.

The court then correctly held that one of the policy objectives was met by the Commission's interpretation in this case (Pet. App. 9a):

> If it had allowed life-of-lease contracts preceded by fixed-term contracts with other parties to qualify for rollover treatment, the Commission would have increased the number of contracts qualifying for the higher ceiling rate. This would have hastened the phase out of

vintaging but, for that very reason, would have increased those economic dislocations to consumers that the Commission sought to ameliorate. It was not irrational for the Commission to decline to pursue this course. Accordingly, the petitioner's policy-related argument is without merit.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

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